



LIBRARY OF CONGRESS

Copyright Royalty Board

[14-CRB-0002-NSR (2016-2020)]

Determination of Royalty Rates for New Subscription Services for Digital Performance Right in Sound Recordings and Ephemeral Recordings

AGENCY: Copyright Royalty Board, Library of Congress.

ACTION: Notice announcing commencement of proceeding with request for Petitions to Participate.

SUMMARY: The Copyright Royalty Judges announce the commencement of the proceeding to determine the rates and terms for the use of sound recordings in transmissions made by new subscription services and for the making of ephemeral recordings necessary for the facilitation of such transmissions for the period beginning on January 1, 2016, and ending on December 31, 2020. A party wishing to participate in this rate determination proceeding must file its Petition to Participate and the accompanying \$150 filing fee by the deadline in this notice.

DATES: Petitions to Participate and the filing fee are due no later than [INSERT DATE 30 DAYS AFTER THE DATE OF PUBLICATION IN THE **FEDERAL REGISTER**].

ADDRESSES: Participants must submit a Petition to Participate in a hard-copy original, with five paper copies and an electronic copy in Portable Document Format (PDF) on a Compact Disc, along with the \$150 filing fee, to the Copyright Royalty Board by either mail or hand delivery. Participants may not submit Petitions to Participate and the \$150 filing fee by an overnight delivery service other than the U.S. Postal Service Express Mail. If participants choose to use the U.S. Postal Service (including overnight delivery), they must address their submissions to: Copyright Royalty Board, P.O. Box 70977, Washington, DC 20024-0977. If participants choose hand delivery by a private party, they must deliver the submissions to the

Library of Congress, James Madison Memorial Building, LM-401, 101 Independence Avenue, SE., Washington, DC 20559-6000. If participants choose delivery by a commercial courier, they must deliver the submissions to the Congressional Courier Acceptance Site, located at 2nd and D Street, NE., Washington, DC. The envelope must be addressed to: Copyright Royalty Board, Library of Congress, James Madison Memorial Building, LM-403, 101 Independence Avenue, SE., Washington, DC 20559-6000.

FOR FURTHER INFORMATION CONTACT: LaKeshia Keys, CRB Program Specialist, by telephone at (202) 707-7658 or email at crb@loc.gov.

SUPPLEMENTARY INFORMATION:

Background

Section 114(f)(2)(C) of the Copyright Act, title 17 of the United States Code, provides that a copyright owner of sound recordings or an eligible nonsubscription service or a new subscription service may file a petition with the Copyright Royalty Judges (Judges) requesting the determination of reasonable terms and rates of royalty payments for a new type of eligible nonsubscription service or a new subscription service on which sound recordings are performed that is or is about to become operational. Upon receipt of such a petition, the Judges must commence a proceeding to determine such reasonable terms and rates by publishing a notice in the **Federal Register**. 17 U.S.C. 803(b)(1)(A)(i)(III), 804(b)(3)(C)(ii).

In 2005, the Judges received a petition requesting that reasonable rates and terms be set for a new type of subscription service that “performs sound recordings on digital audio channels programmed by the licensee for transmission by a satellite television distribution service to its residential customers, where the audio channels are bundled with television channels as part of a ‘basic’ package of service and not for a separate fee”; the Judges commenced a proceeding as

required by section 804(b)(3)(C)(ii). *See* 70 FR 72471, 72472 (Dec. 5, 2005). The Judges adopted the rates and terms agreed to by the parties to that proceeding¹; those rates expired on December 31, 2010. *See* 72 FR 72253 (Dec. 20, 2007).

In order to have successor rates and terms in place prior to the expiration of those rates, the Judges, in 2009, commenced the rate determination proceeding for the 2011-2015 period for the new subscription service as defined in § 383.2(h). *See* 17 U.S.C. 804(b)(3)(C), 74 FR 319 (Jan. 5, 2009). The parties reached agreement regarding the rates and terms for the 2011-2015 license period and the Judges adopted them in 2010. *See* 75 FR 14074 (Mar. 24, 2010). With the current rates set to expire on December 31, 2015, the Judges, by this notice, commence the rate proceeding for the license period 2016-2020. *See* 17 U.S.C. 803(b)(1)(A)(i)(III), 804(b)(3)(C).

Scope of Proceeding

In addition to all other submissions and arguments required by the Act and the applicable regulations, and in addition to any other submissions or arguments that the Participants choose to make, the Judges note below certain potential matters that the Participants may elect to address in this proceeding.

The Judges are open to receiving evidence, testimony, and argument regarding any reasonable rate structure that a Participant may elect to propose, such as, *inter alia*, a rate structure based on the number of subscribers or a percentage of webcaster revenue. This openness is consistent with the determination in *Web II*, 72 FR at 24089,² in which the Judges held that, although the record did not support a percentage-of-revenue based royalty, “[t]his does

¹ The rates are codified at 37 CFR Part 383.

² *Digital Performance Right in Sound Recordings and Ephemeral Recordings, Final rule and order*, 72 FR 24084 (May 1, 2007), *aff’d in relevant part sub nom. Intercollegiate Broad. Sys. v. Copyright Royalty Bd.*, 574 F.3d 748 (D.C. Cir. 2009)(*Web II*).

not mean that some revenue-based metric could not be successfully developed as a proxy for the usage-based metric at some time in the future” The Judges make particular note of this holding in *Web II* because they recognize that, as a practical and strategic matter, participants in these proceedings carefully consider prior rate proceedings as roadmaps to ascertain the structure of the rates they propose.

Pursuant to 17 U.S.C. 114(f)(2)(B), “[i]n determining ... rates and terms the Copyright Royalty Judges shall base their decision on ... *information presented by the parties*” (emphasis added). Thus, the Judges are best served if the participants, their economic witnesses, and their counsel craft arguments in a manner that assists the Judges in identifying and applying the optimal economic analysis when establishing rates and terms pursuant to the Act. As a former federal appellate jurist has noted:

The truism that judicial analysis, economic or otherwise, takes place only in the context of lawsuits between two or more parties imposes a practical constraint on the judge's ability to use economic analysis.... [A] judge will, for the most part, be limited by what the parties serve up to her.

Patricia Wald, *Limits on the Use of Economic Analysis in Judicial Decisionmaking*, 50

Duke J.L. & Contemp. Prob. 225, 228 (1987).

Accordingly, the Judges invite Participants, within the written direct statements, written rebuttal statements, proposed findings of fact and conclusions of law, and through their witnesses and attorneys, as appropriate, to consider addressing the following questions.³

³ Nothing in this section should be construed as a statement by the Judges that any evidence or testimony proffered will be ultimately deemed admissible, competent, relevant, probative, or dispositive as to any issue, or that the Judges will ultimately consider, accept, or adopt any argument made in response to this section. Additionally, nothing in this section should be construed as an indication that the Judges will consider ultimately any of these issues in any determination rendered by them. Finally, by soliciting information regarding these issues, the Judges are not indicating that they have reached any preliminary decisions as to any of these issues.

1. What is the Importance, if any, of the Presence of Economic Variations among Buyers and Sellers?

Web II contains the following observation.

In the hypothetical marketplace we attempt to replicate, there would be *significant variations, among both buyers and sellers*, in terms of sophistication, *economic resources, business exigencies, and myriad other factors*.

Web II, 72 FR at 24087 (emphasis added). This statement echoed the Librarian’s finding in *Webcaster I (Web I)*⁴ that a marketplace unconstrained by a statutory license would experience “a range of negotiated rates” *Web I*, 67 FR at 45244.

If the marketplace indeed would establish multiple rates, the adoption of a rate structure consistent with that result might be more realistic than a single per-performance rate. When such “significant variations” exist, especially among “willing buyers,” each buyer may place a different economic value on a performance. To *impose* a rate that is economically appropriate for *one such willing buyer upon any or all other willing buyers* might not necessarily satisfy the statutory requirement of replicating the marketplace, but rather might be inconsistent with the rate structure of an actual market for sound recordings. Thus, the Judges invite the Participants to address in their proffered evidence, testimony, and/or arguments whether any economic variations among commercial webcasters might affect the selection of an appropriate rate structure.

2. Should Royalty Rates Embody any Form of Economic “Price Discrimination” in order to Reflect the Statutory Hypothetical Marketplace?

In *Web II*, the Judges set forth a concise and accurate summary of market circumstances in which price discrimination—and therefore multiple prices for the same good or service—will arise:

⁴ *Determination of Reasonable Rates and Terms for the Digital Performance of Sound Recordings and Ephemeral Recordings, Final rule and order*, 67 FR 45240 (July 8, 2002)(*Web I*).

A segmented marketplace may have multiple equilibrium prices because it has multiple demand curves for the same commodity relative to a single supply curve.... In other words, *price differentiation or price discrimination* is a feature of such markets. The multiple demand curves represent distinct classes of buyers and each demand curve exhibits a different price elasticity of demand.... Typically, the submarket characterized by lesser price elasticity will exhibit a higher price. All the economists who testified in this proceeding, for both the Services and the copyright owners generally agreed with this description.

72 FR at 24097 (emphasis added); *see also Web I*, 67 FR at 45258 (“economic differences between ... businesses” would cause a per-performance rate appropriate for one type of business “to overstate the market value” of a performance for another type of business).⁵

“[A] seller price discriminates by charging different prices to buyers when the price difference cannot be explained by a cost difference in supplying the copyrighted work.” Michael Meurer, *Copyright Law and Price Discrimination*, 23 Cardozo L. Rev. 55, 58 (2001); *see also* Jean Tirole, *The Theory of Industrial Organization* 133-34 (1988) (“Price discrimination reflects differences in the mark-up of price over marginal cost across sales.”); Harold Demsetz, *The Private Production of Public Goods*, 13 J. Law & Econ. 293, 303-04 (1970) (“There is no single price that can satisfy all equilibrium requirements... under the condition that differences in demand prices can be identified at relatively low cost.... [C]ompetitively produced public goods lend themselves to price discrimination.”); Paul Samuelson, *Aspects of Public Expenditure Theories*, 40 The Rev. of Econ. & Statistics, 332, 336 (1958) (when attempting to price additional copies of public goods with marginal costs approximating zero “the easy formulas of classical economics no longer light our way.”); *see generally* William Baumol, *Regulation Misled by Misread Theory* 6 (AEI-Brookings Joint Center Distinguished Lecture Award Monograph 2006) (“[U]nder common conditions, firms will adopt price discrimination as their

⁵ The Judges understand the foregoing statements in *Web I* and *Web II* regarding price discrimination to explain why rates for noncommercial webcasters were lower than rates for commercial webcasters.

optimal strategy for recoupment of common costs. ... [U]nder competitive conditions, the firm will normally be *forced* to adopt discriminatory pricing wherever that is feasible. Put another way, uniform pricing is *not* to be taken as the normal characteristic of equilibrium of the competitive firm.”) (emphasis in the original).

The Judges invite the Participants to include in their proffered evidence, testimony, and/or arguments a consideration of the potential applicability or inapplicability of price discrimination *within* the commercial webcaster segment of the market as well.

3. What are the Potential Disadvantages of Establishing a Statutory Royalty Rate Not Based on a Per Performance Royalty Rate?

Although there are possible advantages to the establishment of a statutory royalty rate based upon a structure other than a per-performance method, there are potential disadvantages as well. Accordingly, the Judges invite the Participants to include, in their proffered evidence, testimony, and/or arguments, information regarding any potential disadvantages to modifying or departing from a per-performance royalty rate. In response to this question, the Judges invite the Participants to consider the following specific sub-issues.

a. Is It Prohibitively Difficult to Identify Webcaster Revenues for the Purpose of Calculating a Percentage-of-Revenue Based Royalty Rate?

In *Web II*, the Judges described the following three areas in which potential problems existed in the percentage-of-revenue rate proposals presented by the participants in that proceeding: (1) revenue measurement; (2) revenue definition; and (3) auditing and enforcement. 72 FR at 24089-90. The present Judges remain concerned with whether those potential problems would affect any potential use of a percentage-of-revenue based royalty rate. Accordingly, the Judges invite the Participants to include, in their proffered evidence, testimony, and/or

arguments, a discussion of such potential problems and any proposed means to resolve such problems.

b. Is there an “Intrinsic” Value to a Performance of a Sound Recording that is Omitted if a Percentage of Revenue Royalty Rate were to be Adopted?

In *Web II*, the Judges expressed a concern that a percentage-of-revenue based royalty rate would fail to capture the “intrinsic” value of a performance of a sound recording. *Id.* The Judges in *Web IV* are interested in the Participants’ understanding of the “intrinsic” value, if any, of a performance of a sound recording.

Accordingly, the Judges invite the Participants to include, in their proffered evidence, testimony, and/or arguments, a discussion of their understanding of the “intrinsic” value, if any, of a performance of a sound recording, and how it might not be embodied in a royalty rate calculated as a percentage of webcaster revenue.

c. Would a Royalty Rate Calculated as a Percentage of Webcasters’ Revenue be “Disproportionate” to Webcasters’ Use of Sound Recordings?

In *Web II*, the Judges also expressed concern regarding whether a disparity could arise between a royalty rate calculated as a percentage of webcaster royalty and webcaster use of sound recordings. *Id.* The present Judges share that concern.

Specifically, the Judges inquire whether “disproportionality” could arise if some webcasters declined to attempt to maximize profits, and instead attempted to *maximize market share*. Licensors then would suffer the “opportunity cost” of foregone revenues. *Cf.* William Baumol, *The Free Market Innovation Machine* 221 (2002) (licensors must consider not only the marginal dollar cost, but also the “opportunity cost” of granting a licensing to a given licensee). As noted by one of SoundExchange’s economic experts during the proceedings in *Web III*, Dr.

Janusz Ordovery, both of these reactions—profit maximization and market share maximization—would be possible outcomes. Ordovery WRT at ¶¶ 25-26.

The Judges also seek evidence, testimony and argument on whether this risk could be mitigated by combining a percentage-of-revenue based royalty rate with a significant minimum fee. *See* H.R. Rep. No. 105-796, at 85-86 (1998) (Conf. Rep.) (“A minimum fee should ensure that copyright owners are fairly compensated in the event that other methodologies for setting rates might deny copyright owners an adequate royalty. For example ... a minimum fee [should be set] that guarantees that a reasonable royalty rate is not diminished by different types of marketing practices or contractual relationships. ... [I]f the base royalty for a service were a percentage of revenues, the minimum fee might be a flat rate per year (or a flat rate per subscription per year for a new subscription service”) (emphasis added).

Accordingly, the Judges invite the Participants to include, in their proffered evidence, testimony, and/or arguments, a discussion of the problem of “disproportionality” between a royalty rate based upon a percentage of webcaster revenue and the use by webcasters of sound recordings, including the details identified *supra*.

Petitions to Participate

Parties with a significant interest must file Petitions to Participate (PTP) in accordance with 37 CFR 351.1(b)(1). PTPs must be accompanied by the \$150 filing fee in the form of check or money order payable to the “Copyright Royalty Board”; cash will not be accepted.

The Judges will address scheduling and further procedural matters after receiving PTPs.

Dated: December 20, 2013

Suzanne M. Barnett,
Chief Copyright Royalty Judge.

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